



POSTAL REGULATORY COMMISSION

39 CFR Part 3035

[Docket Nos. RM2017-1 and RM2022-2; Order No. 6399]

Competitive Postal Products

AGENCY: Postal Regulatory Commission.

ACTION: Final rulemaking.

SUMMARY: The Commission is adopting a final rule concerning the minimum amount that the Postal Service's competitive products as a whole are required to contribute to institutional costs annually. The rule as adopted uses a formula-based approach to annually calculate competitive products' appropriate share of institutional costs. For additional information, Order No. 6399 can be accessed electronically through the Commission's website at <https://www.prc.gov>.

DATES: Effective [INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

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SUPPLEMENTARY INFORMATION:

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I. Relevant Statutory Requirements

Section 3633(a)(3) of title 39 of the United States Code requires the Commission to “ensure that all competitive products collectively cover what the Commission determines to be an appropriate share of the institutional costs of the Postal Service.” 39 U.S.C. 3633(a)(3). Section 3633(b) requires that the

Commission revisit the appropriate share regulation at least every 5 years in order to determine if the minimum contribution requirement should be “retained in its current form, modified, or eliminated.” 39 U.S.C. 3633(b). In making such a determination, the Commission is required to consider “all relevant circumstances, including the prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products.” *Id.*

II. Background

Pursuant to section 3633(b), the Commission initiated Docket No. RM2017-1 for the purpose of conducting its second review of the appropriate share requirement since the enactment of the Postal Accountability and Enhancement Act (PAEA), Public Law 109-435, 120 Stat. 3198 (2006). In its second review of the appropriate share, the Commission found that market conditions have changed since the PAEA’s enactment and since the Commission’s last review of the appropriate share.¹ As a result, in Order No. 4963, the Commission adopted a final rule implementing a dynamic formula-based approach to setting the appropriate share.²

However, Order No. 4963 was appealed by the United Parcel Service, Inc. and later remanded to the Commission for further consideration by the United States Court of Appeals for the District of Columbia Circuit.³ The court identified two major aspects of Order No. 4963 for the Commission to clarify on remand.

¹ See Docket No. RM2017-1, Order Adopting Final Rules Relating to the Institutional Cost Contribution Requirement for Competitive Products, January 3, 2019, at 4-12, 114-170 (Order No. 4963); see 84 FR 537 (January 1, 2019).

² Order Adopting Final Rules Relating to the Institutional Cost Contribution Requirement for Competitive Products, January 3, 2019 (Order No. 4963). The Final Rulemaking was published in the *Federal Register* on January 31, 2019. See 84 Fed. Reg. 537 (Jan. 31, 2019).

³ *UPS II*, 955 F.3d 1038, No. 19-1026, ECF Document No. 1846181, at 1, (issuing formal mandate), June 8, 2020.

The Commission issued Order No. 6043, which was a supplemental notice of proposed rulemaking that addressed the issues identified by the court and provided an opportunity for interested persons to file initial comments and reply comments concerning the Commission's third 5-year review of the appropriate share as required by 39 U.S.C. 3633(b).⁴ In addition, the Commission issued Order No. 6269, which invited public comment relating to the Commission's analysis pursuant to uncodified section 703(d) of the Postal Accountability and Enhancement Act (PAEA).⁵

The Commission received and considered comments with respect to nearly every aspect of the Commission's findings in Order Nos. 6043 and 6269.

In Section IV., the Commission addresses comments relating to the Commission's statutory interpretation of the appropriate share provisions at 39 U.S.C. 3633(a)(3) and (b). After considering these comments, the Commission has determined not to alter its interpretation as articulated in Order No. 6043, which the Commission continues to conclude is consistent with the PAEA's text and structure, as well as its context and legislative history. See Section IV.

In Section V.A., the Commission addresses comments relating to the application of the "uniquely or disproportionately associated" phrase from 39 U.S.C. 3633(b) to the Postal Service's accrued costs. The Commission continues to find that all attributable costs are already included in the 39 U.S.C. 3633(a)(3) price floor and are furthermore implicitly considered as part of the formula. See Section V.A.2.b. The price floors set under 39 U.S.C. 3633(a)(1)

⁴ Supplemental Notice of Proposed Rulemaking and Order Initiating the Third Review of the Institutional Cost Contribution Requirement for Competitive Products, November 18, 2021 (Order No. 6043). The Supplemental Notice of Proposed Rulemaking was published in the *Federal Register* on August 13, 2018. See 86 Fed. Reg. 67,882 (Nov. 30, 2021).

⁵ Notice and Order Providing an Opportunity to Comment on the Commission's Section 703(d) Analysis, September 7, 2022 (Order No. 6269); Postal Accountability and Enhancement Act (PAEA), Pub. L. No. 109-435, Title VII, § 703, 120 Stat. 3198, 3244 (2006).

and (a)(3) fully ameliorate any competitive deficit alleged to be unaddressed by the price floor under 39 U.S.C. 3633(a)(2), and that the use of incremental costs for purposes of the price floors under 39 U.S.C. 3633(a)(1) and (a)(2) is sufficient to prevent subsidization of Competitive products. See Section V.A.3.b. Any further attempt to account for attributable costs as part of the appropriate share would constitute double-counting of those costs that would be economically unsound and potentially harmful to the Postal Service. See Section V.A.4.b. There is no meaningful relationship between unattributed inframarginal costs and Competitive products; there are no costs uniquely or disproportionately associated with Competitive products within currently-existing institutional costs; and using economically sound measurement is reasonable. See Sections V.A.5.b., V.A.6.b., V.A.7.b. The arbitrary allocation of institutional costs to Competitive products would contravene the intent of the PAEA, would be economically unsound, would degrade the existing costing methodology, and could harm the Postal Service and consumers. See Section V.A.8.b.

In Section V.B., the Commission addresses comments relating to the prevailing competitive conditions in the market and other relevant circumstances. The Commission confirms that revenue is the appropriate measure of market size, and that the profitability of competitors is relevant to assessing the prevailing competitive conditions in the market. See Section V.B.2.b. The Commission presents an updated market analysis and continues to find that the state of competition in the market for competitive postal services is healthy. See *id.*

With respect to comments suggesting that the Commission should consider the Postal Service's financial losses, the "non-existence of a level playing field" and "subsidization," the Commission explains why these three

potential circumstances are not relevant to this review. See Section V.B.3.b.

The Commission finds that comparative harm and the balance of risk and actual Competitive product contribution to institutional costs are relevant circumstances which all weigh in favor of readopting the dynamic formula-based approach. See *id.* Finally, the Commission reiterates its dismissal of comments alleging that the formula is arbitrary and capricious. See Section V.B.4.b.

In Section VI. the Commission addresses comments regarding the Commission's analysis pursuant to uncodified section 703(d) of the PAEA. See PAEA 703(d). In accordance with that provision, the Commission invited additional public comment regarding Commission updates to a quantification by the Federal Trade Commission (FTC) of the net economic effect of federal and state laws that apply differently to the Postal Service than to private competitors in the market for competitive postal services, based on subsequent events that the Commission found affected the ongoing validity of the FTC's findings. See Order No. 6269. The Commission concludes that the additional events (beyond those identified by the Commission in Order No. 6269) raised by commenters are outside the scope of the Commission's 703(d) analysis. See Section VI.C.

In Section VII., the Commission addresses arguments relating to each specific type of costs alleged by any commenters to be uniquely or disproportionately associated with Competitive products. Upon consideration of each category of costs raised, the Commission concludes that none of these costs raised by commenters are uniquely or disproportionately associated with Competitive products and that it would be inappropriate to alter the formula-based approach to take these cost categories into account. See Section VII.

In Section VIII. the Commission addresses comments proposing alternatives to the formula-based approach to setting the appropriate share. The

Commission concludes that UPS's four alternative proposals would each involve the arbitrary allocation of institutional costs to Competitive products, and furthermore all suffer from numerous methodological flaws and inconsistencies with the PAEA. See Sections VIII.A.3., VIII.B.3., VIII.C.3., VIII.D.3. With respect to comments that the appropriate share should be eliminated, the Commission reiterates that it has, pursuant to the discretion accorded to it by 39 U.S.C. 3633(b), elected to retain the appropriate share requirement as a margin of safety against any possibility of the Postal Service having an unfair competitive advantage. See Section VIII.E.3.

Based on the analysis provided above and its review of comments, the Commission readopts its dynamic formula-based approach to calculating the appropriate share.

III. Basis and Purpose of the Final Rule

The purpose of the Commission's formula-based approach is to provide an objective basis on which to quantify the statutory considerations of section 3633(b) in order to determine the year-to-year change in competitive products' joint minimal capacity to generate profit that can be contributed to the coverage of institutional costs. Order No. 6399 at 114.

The formula seeks to determine the Postal Service's overall market power by measuring its absolute and relative market power. *Id.* at 115-117. In order to assess the Postal Service's absolute market power and its market position, the formula utilizes two distinct components. *Id.* The first component is the Competitive Contribution Margin, which measures the Postal Service's absolute market power. *Id.* at 115. Specifically, the Competitive Contribution Margin is calculated by subtracting the total attributable costs of producing the Postal Service's competitive products collectively from the total amount of revenue the

Postal Service is able to realize from those competitive products collectively in a given fiscal year, and then dividing this result by the total competitive product revenue. *Id.* The formula assesses the year-over-year percent change in the Competitive Contribution Margin to determine how much, if any, the Postal Service's absolute market power has changed. *Id.*

The second component of the formula is the Competitive Growth Differential, which measures the Postal Service's market position. *Id.* at 116-117. Specifically, the Competitive Growth Differential is calculated by subtracting the year-over-year percent change in the combined revenue for the Postal Service's competitors from the year-over-year percent change in the Postal Service's competitive product revenue. *Id.* at 116. This relative growth is then weighted by the Postal Service's market share. *Id.*

Using the above-described components, the Commission's formula is represented by the following equation:

$$AS_{t+1} = AS_t * (1 + \% \Delta CCM_{t-1} + CGD_{t-1})$$

$$\text{If } t = 0 = \text{FY 2007, } AS = 5.5\%$$

Where,

AS = Appropriate Share

CCM = Competitive Contribution Margin

CGD = Competitive Growth Differential

t = Fiscal Year

Id. at 117.

In order to calculate an upcoming fiscal year's appropriate share percentage (AS_{t+1}), the formula multiplies the sum of the prior fiscal year's Competitive Growth Differential and percentage change in the Competitive Contribution Margin ($1 + \% \Delta CCM_{t-1} + CGD_{t-1}$) by the current fiscal year's

appropriate share (AS_t). *Id.* at 118. Both components of the formula are given equal weight. *Id.* The formula is recursive in order to incorporate all changes in the parcel delivery market since the PAEA was enacted and the appropriate share was initially set. *Id.* at 103. The formula's calculation thus begins in FY 2007 with a beginning appropriate share of 5.5 percent. *Id.* The upcoming fiscal year's appropriate share will be updated by the Commission each year as part of the Commission's Annual Compliance Determination, which is performed pursuant to 39 U.S.C. 3653. *Id.*

IV. Final Rule

In order to implement the Commission's formula, existing § 3035.107(c) is revised. Final § 3035.1077(c)(1) establishes the formula which is to be used in calculating the appropriate share and defines each of the formula's terms. Final § 3035.107(c) states that the appropriate share of institutional costs to be covered by competitive products set forth in that rule is a minimum contribution level. Final § 3035.107(c)(2) establishes the process by which the Commission shall update the appropriate share for each fiscal year. The Commission will annually use the formula to calculate the minimum appropriate share for the upcoming fiscal year and report the new appropriate share level for the upcoming fiscal year as part of its Annual Compliance Determination.

List of Subjects for 39 CFR Part 3035

Administrative practice and procedure.

For the reasons stated in the preamble, the Commission amends chapter III of title 39 of the Code of Federal Regulations as follows:

PART 3035—REGULATION OF RATES FOR COMPETITIVE PRODUCTS

1. The authority citation for part 3035 continues to read as follows:

Authority: 39 U.S.C. 503; 3633.

2. Amend § 3035.107 by revising paragraph (c) to read as follows:

§ 3035.107 Standards for Compliance.

* * * * *

(c)(1) Annually, on a fiscal year basis, the appropriate share of institutional costs to be recovered from competitive products collectively, at a minimum, will be calculated using the following formula:

$$AS_{t+1} = AS_t * (1 + \% \Delta CCM_{t-1} + CGD_{t-1})$$

Where,

AS = Appropriate Share, expressed as a percentage and rounded to one decimal place

CCM = Competitive Contribution Margin

CGD = Competitive Growth Differential

t = Fiscal Year

If t = 0 = FY 2007, AS = 5.5 percent

(2) The Commission shall, as part of each Annual Compliance Determination, calculate and report competitive products' appropriate share for the upcoming fiscal year using the formula set forth in paragraph (c)(1) of this section.

By the Commission.

Erica A. Barker,

Secretary.